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BY THE COMPTROLLER GENERAL

Report To The Congress

OF THE UNITED STATES

New U.S. Valuation System For Imported Products Is Better And Easier To Administer

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The prior U.S. valuation system for imported products was confusing to importers and expensive for the U.S. Customs Service to administer. The Trade Agreements Act of 1979 provided a new simplified system which has substantially resolved the valuation problems of the prior system.

The new system provides more uniform methods--one primary and four secondary--of determining customs value for the purpose of applying duties. Use of these methods has (1) helped both Customs and the international trade community determine with more certainty the customs value and the amount of duties on imported products and (2) resulted in reduced operating costs

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COMPTROLLER GENERAL OF THE UNITED STATES
WASHINGTON D.C. 20548

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The President of the Senate and the
Speaker of the House of Representatives

This report describes the new U.S. valuation system for imported products and discusses the effectiveness of its implementation. This review was made to evaluate the impact of the new valuation system on the U.S. Customs Service, the importers, and customs brokers.

We are sending copies of this report to the Director, Office of Management and Budget; the Secretary of the Treasury; the United States Trade Representative; the Commissioner, U.S. Customs Service; and cognizant congressional committees.

Charles A. Bowsher

Comptroller General
of the United States

COMPTROLLER GENERAL'S
REPORT TO THE CONGRESS

NEW U.S. VALUATION SYSTEM FOR IMPORTED PRODUCTS IS BETTER AND EASIER TO ADMINISTER

D I G E S T

The consistency of the method of valuation--the process of determining a unit value for imported products--which a country applies can be as important as the tariff rate itself in determining the amount of duty charged. The U.S. Customs Service, an agency of the Department of the Treasury, administers the U.S. valuation system.

Changes simplifying the U.S. valuation system have substantially resolved both Customs' and the importers' concerns about the prior system, which involved nine valuation standards. The prior valuation standards were confusing to importers and expensive for Customs to administer.

The U.S. valuation system has been simplified and made more specific by establishing one primary method--transaction value--and four secondary methods for determining customs value. Under the transaction value method, Customs accepts the price agreed to between the buyer and seller--invoice price, for example--as the basis for customs valuation, as compared to the more complex valuation procedures of the prior system.

The new valuation methods, which went into effect in July 1980, have resulted in two major benefits:

--The customs value of imported products and the amount of duties can be determined with more certainty by both the international trade community and Customs under the new valuation system. The certainty as to the impact of customs duties is an economic consideration in price negotiations for products sold in international trade. (See pp. 5 and 6.)

--The preparation and processing costs for the entry documentation on imported products have been reduced. Customs, importers, and customs

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brokers have been able to process entries more quickly because the valuation procedures are more specific and uniform under the new valuation system.

Simplifying the valuation system has also reduced the number of incorrect entries and resulted in fewer Customs billings for additional duties or refunds. If the estimated reduction in the number of incorrect entries is fully attributed to the new valuation system, the simplification has resulted in an estimated savings of $960,000 by Customs for fiscal year 1981. These savings do not reflect the costs of Customs' training programs and seminars for the new system. (See pp. 6 to 9.)

Customs' training programs and seminars contributed significantly to the successful implementation of the new valuation system. (See pp. 9 and 10.)

GAO provided a draft of this report to Customs officials for comments. Customs officials advised GAO that they agreed with GAO's findings and conclusions.

WHY THE REVIEW WAS MADE

GAO conducted this review to evaluate the impact of the new U.S. valuation system on both Customs and importers. Specifically, GAO was concerned with the efficiency and effectiveness of the new valuation methods in the preparation and processing of entry documentation for imported products.

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CHAPTER 1

INTRODUCTION

Under the Tariff Act of 1930, as amended, the U.S. Customs Service, an agency of the Department of the Treasury, is responsible for enforcing laws pertaining to imported products. Customs determines the value of imported products, assesses and collects duties, and gathers import statistics.

CUSTOMS VALUATION

Valuation--determining a unit value for imported products according to statutory requirements--is carried out by Customs' import specialists. They appraise products, make comparisons with values shown on entry documentation for similar products, examine the importers' records, and use catalogs, price lists, and other sources. Duties are assessed on the basis of an amount per unit (specific rate), a percentage of unit value (ad valorem rate), or a combination of specific and ad valorem rates (compound rate). The method of valuation which a country applies can be as important as the tariff rate itself in determining the amount of duty charged.

Customs processed 4.6 million formal entries--import transactions exceeding $250 in value--of imported products during fiscal year 1981. About 66 percent of these entries were subject to customs duties, generally levied on an ad valorem or compound rate basis. Import duties collected were about $9.2 billion.

PRIOR U.S. VALUATION SYSTEM WAS CONFUSING AND EXPENSIVE TO ADMINISTER

Prior to July 1, 1980, the U.S. valuation system included nine valuation standards--guidelines used to determine product value. The standard used to determine value depended on both the product and the circumstances under which the product was imported. In a previous GAO report, 1/ we pointed out that the valuation standards were confusing to importers and expensive for the Customs Service to administer. The standards were also the source of much litigation and were often inconsistent with commercial trade practices.

The prior U.S. valuation system had long been criticized by many of the United States' trading partners as being a major nontariff barrier to trade. The primary complaint was the amount

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1/Report on "Changes Needed In U.S. Valuation System For Imported Merchandise" (GGD-79-29, Mar. 23, 1979).

of uncertainty and complexity built into the valuation system. U.S. importers believed it was frequently impossible to foresee under which of the nine valuation standards their products would be appraised. Foreign exporters held the same belief.

While the prior U.S. valuation system had been criticized, the customs valuation systems of the United States' trading partners also had controversial and protective features. It was against this background that international rules for uniform customs valuation were developed during the Tokyo Round of multilateral trade negotiations. The objective of the trade agreement concerning customs valuation was to ensure that these new rules are fair and simple, conform to commercial reality, and allow traders to predict, with a reasonable degree of accuracy, the duty that will be assessed on their products.

NEW VALUATION SYSTEM

The Trade Agreements Act of 1979 approved and implemented the trade agreements negotiated by the United States in the Tokyo Round of multilateral trade negotiations. One of these trade agreements concerned the valuation of imported products. The law sets out one primary method--transaction value--and four secondary methods for determining customs value. These valuation methods, in order of precedence of application, are:

Transaction Value
Transaction Value--Identical Products
Transaction Value--Similar Products
Deductive Value (based on resale price after importation, less certain deductions)
Computed Value (based on production costs, profit, and overhead)

An importer has the option of reversing the order of precedence of the last two methods. If none of the five prescribed methods can be used, the act requires that "the merchandise will be appraised on the basis of a value that is derived from one of the previous methods, adjusted to the extent necessary."

The new valuation system became effective July 1, 1980, and applied to exports to the United States on or after that date. For certain rubber footwear products the effective date was July 1, 1981.

Transaction value method

The transaction value method--the primary method--specifies that customs value shall be the price actually paid or payable for the goods, with additions for certain specified costs, charges, and expenses incurred in the transaction but not included in

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the price. These additions cover such items as selling commissions, packing costs, royalties and license fees, and assists. Assists are assets that the buyer furnishes, either directly or indirectly, to the seller of the products at no or at a reduced cost, which thereby reduces the price at which the seller can sell goods to the buyer. If the transaction value method cannot be used to establish customs value, the other methods are applied in order of precedence.

OBJECTIVES, SCOPE, AND METHODOLOGY

Our review objectives were to (1) evaluate Customs' implementation of the provisions of the Trade Agreements Act of 1979 concerning customs valuation and (2) assess the impact of the new valuation methods on both Customs and the importers and/or their brokers.

Our work was performed at Customs headquarters, Washington, D.C.; the New York Region and the Seaport Area Office, New York, New York; the Boston Region and the Boston District Office, Boston, Massachusetts; and the Buffalo District Office, Buffalo, New York.

We also:

--Reviewed laws, policies, and procedures relating to the processing of formal entries.

--Examined and analyzed entry statistics for fiscal years 1979 through 1981.

--Reviewed the extent and adequacy of the training and guidance provided by Customs officials to both their employees and the importers and/or their brokers in implementing the new valuation system.

--Examined internal and external studies and audits pertaining to the valuation of imports.

This review was performed in accordance with GAO's current "Standards for Audit of Government Organizations, Programs, Activities, and Functions."

Methodology

The Customs regions and districts were selected because of the large entry workload and diversification of imports. Also, the New York regional area is the headquarters for both Customs' national import specialists and some national importer and customs broker organizations. In fiscal year 1981 Customs' New York Region collected $2.5 billion in duties and processed

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718,226 dutiable entries. Boston collected $723 million and processed 512,103 dutiable entries. These two regions processed about 40 percent of all dutiable entries.

Customs' district officials we interviewed included 14 of the 78 national import specialists, 6 of the 14 supervisory import specialists, and 14 of the 79 district import specialists. We also talked with Customs officials at headquarters and the Boston and New York Regions. Broker officials included 4 who represented a national brokers' organization and 10 individual brokers. Importers included 2 officials from a national importer/exporter organization and 12 importers who prepared their own entries without the assistance of a customs broker. All of them were asked their views as to the impact of the new valuation system on their respective operations and whether any reductions in processing time or measurable savings resulted from the use of the new valuation methods.

Although we visited only two of the nine Customs' regional offices, we believe our findings are representative of all regions for several reasons. First, the national import specialists are Customs' focal point for the development and coordination of information to accurately and uniformly value imported products throughout all districts. Second, the views of the Boston and New York regional officials take into consideration the valuation operations in 10 of the 45 Customs districts. Third, Customs headquarters officials, the national customs brokers organization, and the national association of importers are familiar with the impact of the new valuation system. We have no reason to believe that the views on the new valuation system in the other regions and districts would be dissimilar.

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CHAPTER 2

NEW VALUATION SYSTEM FOR IMPORTED PRODUCTS IS LESS CONFUSING AND LESS COSTLY TO ADMINISTER

The new valuation methods have resulted in a uniform, fair, and greatly simplified system for the valuation of imported products. The acceptance and use of the transaction value--the primary valuation method--as the means of determining the customs value for about 94 percent of the formal entries has eliminated the confusion and the inordinate expense of valuation procedures that existed under the prior system. The overwhelming use of the transaction value method has also reduced the entry processing costs for both Customs and the importers and/or their brokers.

TRANSACTION VALUE METHOD USED FOR MOST IMPORTS

The new valuation system is less complex primarily because of the use of the transaction value method. Under this method, Customs can accept the price agreed to between the buyer and seller--invoice price, for example--as the basis for customs valuation, as compared to the determination of value through the use of the more complex valuation procedures of the prior system.

The primary measure of the success of the new valuation system is the extent that the transaction value method is being used. A Customs study regarding the use of transaction value was made at five of its largest districts/offices during October 1981. These locations, the New York Seaport, the New York Kennedy Airport, and the Buffalo, Detroit, and Los Angeles districts accounted for about 50 percent of all the formal entries processed. The study disclosed that the transaction value method was used for about 94.2 percent of the entries that were processed. The percentage use of the other valuation methods was:

--Transaction Value--Identical Products	1.0 percent
--Transaction Value--Similar Products	.5 percent
--Deductive Value	.8 percent
--Computed Value	2.1 percent
--Other	1.4 percent

Automobiles, steel products, shoes, and chemicals are some examples of products for which the customs value is usually based on the transaction value method. The valuation of these products under the prior system was confusing and the application of the old valuation standards was time-consuming and expensive.

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Twenty-eight of the 34 import specialists we interviewed stated that the use of the transaction value method has been the primary reason for the improvement in the valuation system. The remaining six import specialists advised us that because of the type of entries they appraise they have not noticed any extensive improvement. Although precise data were not available, 26 of the 34 import specialists estimated that transaction value was being used about 90 percent of the time. The remaining import specialists either could not provide an estimate or estimated less than 90 percent.

The exporters' and the importers' use of the new valuation system--primarily the acceptance of the transaction value method--has allowed them to determine, with more certainty, both the customs value of imported products and the amount of duties. Thus, the exporters' and importers' use of the transaction value method provides them more certainty as to the economic impact of customs duties in price negotiations for products sold in international trade.

Under the prior system, the importers' valuation of imported products sometimes differed from that of Customs and resulted in billings for additional duties or refunds. The use of the transaction value method has reduced this problem. About 86 percent of the Customs, importer, and broker officials we interviewed said that the primary benefit of the new system was the greater degree of certainty of the amount of customs valuation.

NEW VALUATION SYSTEM HAS REDUCED CUSTOMS', IMPORTERS', AND BROKERS' COSTS

The new valuation system, because of the extent of use of the transaction value method, has resulted in reduced costs of preparing and processing formal entries. The cost savings have benefited both Customs and the importers and/or their brokers.

Customs' costs to administer the valuation system have been reduced

Customs' import specialists have been able to process formal entries more quickly because the valuation procedures are more specific and uniform under the new valuation system. Customs officials advised us that the reduction in the time required to verify the valuation of imported products has allowed Customs personnel to devote more time to duties other than valuation activities. About 4.6 million formal entries were processed during fiscal year 1981, compared to about 4.4 million for the prior fiscal year. Also, under the new system the number of entries with incorrect value information requiring corrective action by import specialists has been reduced.

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Twenty-eight of the 34 import specialists advised us that the valuation of imported products is accomplished faster under the new system because it is less complex. They believe that the time-consuming detailed verification procedures of the prior valuation system have been eliminated. The specialists also believe that, because brokers and importers have a better understanding of the new valuation methods, they make fewer valuation inquiries. Thus, the new valuation system has also allowed import specialists to spend more time on other entry verification procedures such as the classification of imports. The following are some typical examples of the reduction in the import specialists' valuation workload:

--An import specialist advised us that under the new valuation system price lists for certain commodities no longer have to be prepared and circulated around the country. Substantial resources were required for preparation, circulation, and review of these lists under the old system.

--Import specialists advised us they have saved time because they no longer have to maintain, consider, and verify pricing information and sales to other importers when determining a "freely offered price"--a concept used in the prior valuation system.

--An import specialist advised us that importers' use of transaction value--instead of the prior cost of production standard--eliminated the need for duty adjustments for 1,800 or 25 percent of the 7,200 entries processed by this specialist.

--The import specialists in Boston and New York who process footwear entries told us that the elimination of the previously used American selling price valuation standard has reduced their valuation workload.

Number of incorrect entries reduced

The new valuation system has resulted in a reduction in the number of dutiable formal entries requiring corrective action after acceptance by Customs. The amount of the duties deposited by importers/brokers are based on their assumptions as to the customs value and the classification of the imported product. If a valuation or classification error results in an adjustment of $10 or more, Customs either issues a bill for additional duties or a refund check. Customs' officials, importers, and brokers advised us that under the new valuation system the number of incorrect entries had been reduced.

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Our analysis of entry statistics disclosed that the number of incorrect entries has decreased since the new valuation system became effective, as shown in the following table.

Fiscal year	Incorrect entries	Correct entries	Total	Percent of entries incorrect
1979	317,999	2,684,797	3,002,796	10.6
a/1980	344,983	2,771,420	3,116,403	11.1
1981	296,983	3,021,853	3,318,836	8.9

a/Effective date of new valuation system was July 1, 1980.

Although there was an increase of about 202,000 entries from fiscal year 1980 to 1981, the number of incorrect entries decreased by about 48,000. The decrease in the number of incorrect entries as a result of the changes in the method of valuation, however, is understated because of a change in Customs' pre-entry review procedures. Prior to December 1980, entries that contained minor errors were returned to the importer/broker and they were not included in Customs' statistics on incorrect entries. Under Customs' revised pre-entry review procedure entries are returned only if there are substantive errors. Thus, Customs officials advised us that this procedural change probably increased the number of incorrect entries entered into the system.

Our analysis of the entries disclosed that the average percentage of incorrect entries increased during the last three quarters of fiscal year 1981 in comparison to the first quarter. But, the total number of incorrect entries was still less when compared to the corresponding quarters during fiscal year 1980. Twelve of the 14 brokers and 11 of the 12 importers also advised us that there has been a reduction in the number of incorrect entries.

Customs estimated that it cost $20 to issue either a bill for additional duties or a refund check. If the estimated reduction of 48,000 in the number of incorrect entries is fully attributed to the new valuation system, a savings of $960,000 in administrative expenses would have resulted during fiscal year 1981. These savings do not reflect the costs of Customs' training programs and seminars for the new system.

Reduced costs of preparing entries benefits importers and brokers

Importer and broker officials advised us that the new valuation system has reduced the cost of preparing formal entries. Thirteen of the 14 brokers and 7 of the 12 importers advised us

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that the new valuation system has reduced the time needed to determine the customs value of imported products. The other broker and 5 importers said they have not attempted to determine whether costs have been reduced or believed it was too soon to attribute any cost benefits to the new valuation system.

Some examples of cost reductions attributed to the new valuation system include:

--One brokerage firm realized a $10,000 annual savings because it no longer had to prepare and maintain extensive customs valuation data on imported products that was required under the old valuation system.

--Another brokerage firm has saved $1.25 per entry because the valuation system has been simplified.

--One broker advised us that the amount of time spent in discussions with Customs' import specialists on valuation matters has been reduced.

Some of the brokers advised us that the cost reductions enabled them to reduce or limit the amount of increase in the fees charged for preparing formal entries.

Importers who do not use a broker for entry preparation advised us that use of the new valuation system resulted in cost reductions in the preparation of formal entries. Examples include:

--An importer realized annual cost reductions of about $5,000 by having to make fewer changes to internal records concerning valuation data on imported products.

--Another importer's use of the transaction value method resulted in annual savings of $2,400 in entry preparation costs.

--An importer's use of the transaction value method resulted in a 75 percent reduction in the number of entries rejected by Customs, but the cost savings were not estimated.

CUSTOMS SUCCESSFULLY IMPLEMENTED THE NEW VALUATION SYSTEM

Customs' training programs and seminars made a significant contribution to the successful implementation of the new valuation system. Its efforts were efficient and effective and yielded favorable results for both Customs and the international trade community.

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Prior to implementation of the new valuation system, Customs implemented a comprehensive training program to ensure that its import specialists as well as importers and brokers understood the new valuation methods and the procedures to be followed. Customs conducted indepth training courses for import specialists and other employees such as its regulatory auditors. Customs also conducted seminars for all interested importers, brokers, and national and local trade associations. While precise figures were not maintained, a Customs official estimated that over 100 seminars were held or speeches made.

The training program included a Customs booklet which contained a narrative description of the new valuation system, related provisions from the Trade Agreements Act of 1979, and a series of questions and answers concerning the new valuation methods. Customs issued over 19,000 copies of this booklet. A Customs official advised us that the booklet was reprinted by some trade organizations and distributed to its members. Customs also considered a telephone "hot line" for use by the international trade community to obtain valuation guidance on specific imported products. But, because of the training program and sufficiency of communications between Customs' regional and district personnel and the international trade community, Customs concluded that a hot line was not needed.

All of the Customs import specialists and brokers and 9 of the 12 importers we interviewed had attended one of the Customs training programs for the new valuation system. Their consensus was that Customs' efforts resulted in facilitating the transition to the new valuation system.

CONCLUSIONS

The new valuation system has resulted in a uniform, fair, and greatly simplified system for the valuation of imported products. A significant benefit of the new valuation system to both Customs and the importers and/or their brokers has been the degree of certainty in determining both the customs value of imported products and the amount of duties. Changes to the valuation system have saved time and money and improved the efficiency of the preparation and the processing of formal entries. Customs deserves credit for successful implementation of the new valuation system.

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We provided a draft of this report to Customs officials for comments. Customs officials advised us that they agreed with our findings and conclusions.

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